

TEACHERS' RETIREMENT BOARD  
INVESTMENT COMMITTEE

SUBJECT: Alternative Investments  
Activity Status Report

ITEM NUMBER: 14

ATTACHMENT(S): 3

ACTION: \_\_\_\_\_

DATE OF MEETING: May 3, 2000

INFORMATION: X

PRESENTER(S): Réal Desrochers

The table below contains Alternative Investment activity for the month of March 2000 and historical information for selected time periods.

	Month Ended 3/31/00	Fiscal Year To Date	Past One Year	Past Three Years	Past Five Years
<u>Commitments:</u>					
Partnerships	\$ 400,000,000	\$ 1,160,000,000	\$ 1,189,500,000	\$ 3,788,847,013	\$ 4,862,394,629
Co-Investments	0	72,499,996	72,499,996	72,499,996	119,499,996
Secondaries	0	70,773,417	70,773,417	80,067,245	80,067,245
	<b>\$ 400,000,000</b>	<b>\$ 1,303,273,413</b>	<b>\$ 1,332,773,413</b>	<b>\$ 3,941,414,254</b>	<b>\$ 5,061,961,870</b>
<u>Contributions:</u>					
Partnerships	\$ 120,320,720	\$ 1,082,134,690	\$ 1,286,193,749	\$ 2,478,889,402	\$ 3,071,167,804
Co-Investments	0	43,166,685	43,166,685	43,166,685	90,166,685
Secondaries	1,450,000	61,832,402	61,874,044	69,594,231	69,819,231
Mgmt. Fee (Outside)	0	7,629,909	8,295,376	24,746,051	34,835,794
	<b>\$ 121,770,720</b>	<b>\$ 1,194,763,686</b>	<b>\$ 1,399,529,853</b>	<b>\$ 2,616,396,369</b>	<b>\$ 3,265,989,514</b>
<u>Distributions:</u>					
Cash	\$ 73,440,261	\$ 366,811,343	\$ 473,746,126	\$ 1,136,062,105	\$ 1,510,837,992
Stock	128,704,018	719,110,566	764,151,242	1,038,566,535	1,214,739,135
	<b>\$ 202,144,279</b>	<b>\$ 1,085,921,908</b>	<b>\$ 1,237,897,368</b>	<b>\$ 2,174,628,639</b>	<b>\$ 2,725,577,127</b>
Stock Sales	\$ 85,897,756	\$ 576,625,205	\$ 613,175,287	\$ 857,237,229	\$ 1,031,386,651

In accordance with the Alternative Investments Business Plan, this report also presents a summary of the status of the portfolio at the quarter ended March 31, 2000. Attachment 1 presents approved allocations and targets to each Alternative Investment Sub-Category, and shows CalSTRS' current exposure in each of the respective segments.

Attachment 2 contains a summary of investment performance and portfolio exposure by market segment. The venture capital segment, which represents 13.2% of the CalSTRS' portfolio, continues to outperform the other market segments.

Attachment 3 provides an executive summary of action taken under delegation of authority for a commitment of \$400 million to Thomas H. Lee Equity Fund V, L.P. CalSTRS' commitment is subject to the successful negotiation of partnership terms and legal review.

NOTE: Attachments 1 and 2 are not available in electronic format.

Alternative Investments

EXECUTIVE SUMMARY OF ACTION TAKEN  
UNDER DELEGATION OF AUTHORITY  
THOMAS H. LEE EQUITY FUND V, L.P.

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**Action:** Commit \$400 million to Thomas H. Lee Equity Fund V, L.P. (THL V) which represents between 6% - 8% of the total capitalization of the fund.

**Background:** Since its founding in 1974, THL has focused on identifying and acquiring substantial ownership interests in middle market growth companies, has invested approximately \$5 billion of total capital, and has achieved a compound annual internal rate of return on equity invested of approximately 76% as of December 31, 1999. The Firm's investment record and reputation have created a brand name which generates high quality investment opportunities and provides excellent access to the debt and equity capital markets.

CalSTRS is an investor in two previous Thomas H. Lee funds. CalSTRS committed \$100 million to THL III which was established in December 1995, and committed \$150 million to THL IV in February 1998.

**Analysis:** THL V qualifies as a follow-on fund as identified in the Alternative Investments' policies.

The THL investment strategy focuses on middle market companies with enterprise values of \$300 million to \$5 billion which have opportunities for sustainable growth in their core or related businesses. THL targets companies that can capitalize on key competitive advantages to increase cash flow through market growth, market share gains, distribution or product line expansion, and/or market consolidation. Target companies' identifiable strengths include well-recognized brand names, dominant market share positions, unique product features, and/or distribution, manufacturing, or other cost advantages.

THL adds value in managing its portfolio companies by actively working with and building outstanding management teams, incenting them properly, and augmenting them where necessary. THL also consistently enhances portfolio companies' corporate finance capabilities and aggressively creates and manages those companies' acquisition programs. As active Board members, the Firm's partners work closely with portfolio companies' senior management on strategic, financial, and key personnel decisions, pro-actively participating in matters such as identifying cost savings opportunities.

Investment Thesis: Staff is recommending an investment in Thomas H. Lee Equity Fund V for the following reasons:

- Staff has identified Thomas H. Lee as a Tier 1 Manager.
- The THL funds consistently generate investment returns in excess of the Venture Economics upper quartile benchmark.
- Co-investment opportunities will be offered with no fees and no carried interest.
- THL's buy-out strategy is consistent with the targets and ranges which have been approved by the Investment Committee to invest between 50-70% of the Alternative Investment portfolio in buy-out limited partnerships.
- The THL investment strategy provides a good fit in the CalSTRS' portfolio.
- Staff has received a positive investment recommendation from Pathway Capital Management.

Policy Compliance: This decision complies with the portfolio's policies and procedures, which were approved by the Investment Committee on June 3, 1998. A positive written recommendation by the Alternative Investment's advisor and CalSTRS' staff has been documented. This resulted after an investment analysis and due diligence was conducted in the manner as previously reviewed and approved by the Investment Committee.

Recommendation: Staff recommends that CalSTRS commit \$400 million to Thomas H. Lee Equity Fund V, L.P. CalSTRS' commitment is subject to the successful negotiation of partnership terms and legal review.

By:

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Trish Taniguchi  
Investment Officer

Date\_\_\_\_\_

Recommended By:

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Réal Desrochers  
Director of Alternative Investments

Date\_\_\_\_\_

Approved:

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Patrick Mitchell  
Chief Investment Officer

Date\_\_\_\_\_